STATE OF IOWA
PROPERTY ASSESSMENT APPEAL BOARD

O'Charley LLC, Petitioner-Appellant, v. **Dallas County Board of Review,** Respondent-Appellee.	**ORDER** **Docket No. 11-25-0420** **Parcel No. 16-13-402-015**

On March 26, 2012, the above-captioned appeal came on for hearing before the Iowa Property Assessment Appeal Board. The hearing was conducted under Iowa Code section 441.37A(2)(a-b) and Iowa Administrative Code rules 701-71.21(1) et al. Petitioner-Appellant O'Charley, LLC was represented by attorney Dennis P. Ogden of Belin McCormick, P.C., Des Moines, Iowa, and submitted evidence in support of its appeal. The Dallas County Board of Review designated attorney Brett Ryan of Watson & Ryan, PLC, Council Bluffs, Iowa, as its counsel and submitted evidence in support of its decision. The hearing for this appeal was consolidated with the 2010 assessment appeal for the same property. That assessment is addressed in a separate order. The Appeal Board now having reviewed the record, heard the testimony, and being fully advised, finds:

Findings of Fact

O'Charley's, LLC, is the owner of property located at 6240 Mills Civic Parkway, Clive, Iowa. It appeals from the Dallas County Board of Review decision reassessing its property. The real estate was classified commercial for the January 1, 2011, assessment and valued at $1,889,530; representing $1,054,160 in land value and $835,370 in improvement value. O'Charley's protested to the Board of Review on the ground that the property was assessed for more than authorized by law under Iowa Code section 441.37(1)(b). The Board of Review denied the protest.

O'Charley's then appealed to this Board on the same ground. It sought an assessment of $1,300,000. However, at hearing, it submitted an appraisal of the property and now seeks a valuation of $1,500,000.

The subject property is a 5866 square-foot, franchise restaurant with a 738 square-foot, covered, outdoor patio area built in 2007. It is located at the intersection of Mills Civic Parkway and Stagecoach Drive in West Des Moines, and is part of the Galleria at Jordan Creek Development. This development is a 700,000 square-foot community shopping district located along Mills Civic Parkway between 60th and 68th Streets. The improvements are in normal condition and have 2% physical depreciation. The site is 1.210 acres with 30,000 square feet of asphalt paving.

Nancy J. Pearne, Trustee, and Elizabeth Pearne purchased the property in 2006 and transferred it to O'Charley's LLC, a corporation formed for that purpose, in September 2010. As of the January 1, 2011 assessment date, the property was vacant and had been vacant in for roughly two years. A new lease for the property did not occur until September 2011, when Bang Bang Mongolian Grill, a local start-up restaurant, entered into an agreement with the owners. (Exhibits 30). The new 2011 lease has a much lower base rent and shorter term than the initial lease for the property entered into in 2007.

O'Charley's provided profit and loss statements for calendar years 2007 through 2010 (Exhibit 37). The statements showed a continuous decline in actual net operating income (NOI) and an approximately $50,000 loss in 2010. We note the figures provided account for the ground lease payments only, and do not include the building lease payments paid to the owner, Beverly Devin, thus they are unsuitable for comparison in an income approach to valuation.

In further support of its claim, O'Charley's submitted an appraisal[1] completed by Fred H. Lock and Tasha K. Gould[2] of Iowa Appraisal and Research Corporation, Des Moines, Iowa (Exhibits 1-29). Lock also testified at hearing. The Lock appraisal establishes a reconciled fee simple market value for

[1] The Lock and Gould appraisal is hereafter referenced as Lock's appraisal.
[2] Robert D. Blincow was also identified as an appraiser on another version of the report included in the certified record.

the subject property for January 1, 2011, after considering all three valuation approaches: cost, sales comparison, and income. His values are as follows:

	2011 Value
Cost Approach	$2,100,000
Sales Comparison Approach	$1,600,000
Income Approach	$1,400,000
Reconciled Value	$1,500,000

The appraisal notes "new construction in the [subject's] neighborhood has slowed recently due to the national recession. With the recent development of West Glen Town Center and the Village of Ponderosa there is an oversupply of office and retail development, some of which has been vacant for over a year." (Lock Appraisal p. 14).

Lock's Cost Approach

Lock developed the cost approach to value and determined a value of $2,100,000 (rounded) for 2011 assessment year. Lock stated the effective age of the property is 3 years, with a remaining economic life of 42 years. He valued the land at $1,110,000 based on six land sales, which all occurred on Mills Civic Parkway in West Des Moines and includes the 2006 sale of the subject property. Two sales occurred in 2005, three in 2006, and one in 2008. Lock testified he was unable to locate any more recent, comparable land sales. The sales appear quite similar in size to the subject property. Adjustments were made for location and size. The appraisal concludes an adjusted land value per square foot for the subject property ranging from $19.44 to $20.66. He then reconciled to the high end of the range at $21.00 because the subject property's corner site at the entrance to the Galleria community shopping center.

Lock valued the improvements at $885,917 using *Marshall Valuation Service* and then applied a 6.7% adjustment for physical depreciation, resulting in a depreciated cost of $826,561. He also indicated his belief that the improvements suffers from obsolescence. He notes "[t]he subject was constructed as a build to suit restaurant where the original tenant failed and current market rents do not support the cost of construction. A future investor would likely consider the cost approach to have minimal weight." (Lock Appraisal p. 24).

Lock's Sales Approach

In the sales comparison or market approach to value, Lock used seven sales of restaurants in Clive, Urbandale, Ankeny, and West Des Moines that ranged in size from 4968 square feet to 8802 square feet. The sales prices ranged from $511,190 to $3,400,000 or $100.12 per square foot to $386.28 per square foot, and occurred between February 2003 and January 2011. Adjustments were made for market conditions, location, age/condition, quality/design, and land-to-building ratio.

Lock notes there were limited recent transactions to provide good comparables for the subject property. "The most recent two sales were of the leased fee estate with long term leases in place to national franchise restaurant chains." (Lock Appraisal p. 29). He included some older data of fee simple transactions and considered a secondary set of fee-simple transactions outside the subject property's area.

The appraisal notes that Sale 1 (1220 NW 128th Street, Clive), Sale 2 (4502 University Avenue, West Des Moines), Sale 4 (1310 NW 118th Street, Clive) and Sale 5 (4810 NW 86th Street, Urbandale) sold with leases in place but no adjustments were required because they were "at market level." Locke testified that leased-fee properties, however, typically sell for higher value than fee simple properties. The appraisal indicates it was difficult to determine appropriate adjustments for market conditions. It notes, however, the existence of a property currently listed for sale at a price below the 2007 sale price, which has been on the market for a year. Lock additionally reports that retail market deteriorated in the recent "Great Recession" and investors expect higher capitalization rates. He indicates construction has slowed and vacancy rates have risen as well indicating that values declined. In his opinion, this theory is further supported by evidence of declining rents.

Lock also reviewed five fee simple sales from Sioux City and Sioux Falls, Iowa. The properties were all built as a franchise restaurant like the subject, but now are occupied by a different user. After market adjustments, these sales ranged between $118.73 and $321.93 per square. He concluded the range indicated by these sales supports the range of indicated values of the local fee-simple sales and demonstrates higher per-square-foot values for leased-fee estates.

Additionally, Lock provided five local full service restaurants listings all priced between approximately $150 and $170 per square foot. These also support the sales range of the majority of the fee simple sales.

Based on the seven local sales, and after considering the secondary sales data set and listings, Lock concluded $270 per square foot was an appropriate value for the subject property. The total value indicated by the sales comparison approach was $1,600,000 (rounded).

Lock's Income Approach

In the income approach to value, Lock estimated the market rent using six leases of property in West Des Moines, Ankeny, and Des Moines. Estimated market rent assumed the tenant pays all expenses except miscellaneous landlord expenses, a replacement reserve, and leasing costs. The rates were adjusted for market conditions, location, size, tenant improvement allowance, and land/building ratio. The adjusted leases rates ranged from $17.80 per square foot to $31.08 per square foot. Market rates were then adjusted for vacancy allowance at 5%. Lock arrived at this figure because although there has been a steady decrease in occupancy in the subject property's submarket, he predicts the subject property will experience a vacancy rate below that indicated by the survey due to its excellent location and visibility on a corner site. Adjustments were also made for collection loss, management fees, leasing fee, and replacement reserves to determine an NOI of $135,380.

Lock then determined a cap rate to apply to the net operating income. He extracted cap rates from six leased restaurants in the Des Moines Metro area. He noted he had observed that capitalization rates for retail properties have been increasing and it is likely that a prospective purchaser of the subject would expect a higher capitalization rate than is indicated by the leased-fee sales, which ranged from 7.95% to 10.92% (before reserves). He further noted that comparable 4 currently is listed on the market with an overall cap rate of 13.5%. Lock also considered a loan-equity analysis. He then considered a cap rates from surveys published in RealtyRates.com that averaged 13.64% for full-service restaurants. Lock reconciled to a 9.25% cap rate, then used an adjusted cap rate of 9.43%. Lock concluded this cap rate was appropriate because the local market called for a lower rate than the national rate, but higher than the sales of leased-fee properties.[3] Using this rate, the subject property's estimated value is $1,400,000.

In determining a reconciled value for the subject property, Lock considered the sales approach reliable and gave it weight in the final analysis. He commented that properties similar to the subject are generally purchased based on their income producing potential. He considered the income approach to be the most appropriate valuation method for the subject. Lock gave less consideration to the cost approach because it trended higher that the other two approaches indicating obsolescence or lack of a financially feasible use. Lock concluded a final reconciled value of $1,500,000 as of January 1, 2011.

The Board of Review submitted an appraisal[4] completed by Gene F. Nelson and Ranney Ramsey of Nelsen Appraisal Associates, Inc., Urbandale, Iowa (Exhibit C). Ranney Ramsey also testified on behalf of the Board of Review. Ramsey valued the subject property at $1,700,000 as of January 1, 2011. Like Lock, Ramsey completed all three approaches to value. While Ramsey found the subject property was assessed for greater than its market value, his final conclusion of value is higher than Lock's. His conclusions and reconciled values are as follows:

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[3] We note Lock's cap rate decreased for 2011 as compared to an appraisal he completed on the subject property for 2009-2010. During that period (2009-2010) Lock found the cap rate was increasing. Lock justified the decrease in cap rate for 2011 based on some sales in the local market, albeit they were leased-fee transactions.
[4] This appraisal is hereafter referenced as the Ramsey appraisal.

	2011 Value
Cost Approach	$ 1,725,000
Sales Comparisons Approach	$ 1,750,000
Income Approach	$ 1,650,000
Reconciled	$ 1,700,000

Like Lock, Ramsey reported the subject property is located on Mills Civic Parkway near Interstate-35 and Interstate-80, an immerging dominant retail area in the Des Moines metropolitan area. He further notes the property's proximity to the Jordan Creek super-regional mall, Wells Fargo corporate campus, Aviva Insurance headquarters, Super-Target, Wal-Mart Super Center, and another power center on the Mills Civic Parkway corridor, as well as several new national chain hotels. Ramsey states the area is a relatively affluent trade area based on median household incomes, has forecasted growth of about 2-3% per year from 2010 to 2015, and average net worth. Ramsey indicates the Restaurant Performance Index demonstrated a pattern of steep decline beginning in mid- to late 2007 and continuing to January 2009 followed by a pattern of increases continuing into the middle of 2011.

Ramsey's Cost Approach

Ramsey developed the cost approach to value and determined a value of $1,725,000 for 2011. He valued the land at $1,050,000 based on five land sales on Mills Civic Parkway in West Des Moines. All five of these land sales were also used by Lock in his appraisal. Ramsey adjusted the sale prices, and then concluded a most likely value of $20 per square foot for the property. He further reduced this value due to the decline in land values by using an adjusted cost multiplier to reflect what they considered "holding periods" in the market. Ramsey testified that national surveys indicated a slump in restaurant sales between 2008 and 2010, with some improvement in 2011. He reported the local market may be saturated with restaurants and that there is no immediate need for land. Because of this, there are no recent land sales and a holding period would be likely. Therefore, land purchases would be speculative and buyers would want more discounting. For 2011, he applied a multiplier of 0.917 to reflect one year of holding time. His land value conclusion was $965,000 (rounded).

The improvements were valued using *Marshall Valuation Service*, similar to Lock's appraisal. Ramsey determined an effective age of 3 years for 2011 and a remaining economic life of 52 years. Ramsey valued the improvements at $761,238 after deductions of 5.5% for physical depreciation.

Ramsey's Sales Approach

In the sales comparison approach, Ramsey examined both leased-fee and fee simple sales.[5] He noted that most fee-simple sales from one restaurant to another tended to be older transactions involving older facilities. He was concerned relying only on these results "could bias the result downward." (Ramsey Appraisal p. 67). Therefore, Ramsey determined it was also appropriate to consider leased-fee sales. He contend that if the terms of the lease at the time of sale produce an income similar to the income of the property at market conditions and if the terms of the lease are similar to those that would exist in an open and competitive market, the transactions can be useful. However, he also pointed out that "the leased fee interest may have guarantees and provisions that provide financial benefits that are above and beyond the fee simple . . . [and] could bias the results upward." (Ramsey Appraisal p. 67). Ramsey testified that properties subject to leased-fee have an assured income stream and higher values and that fee simple properties, which are typically older, have lower values. He also noted the ability of the tenant to pay rent determines value with national chains having greater ability to pay. He testified the leased-fee properties sold for higher value than fee-simple properties.

Ramsey identified six restaurant sales in Clive and West Des Moines. Three of the properties were local restaurants, which represented the oldest sales from 2003 to 2005, and appear to be the fee-simple sales; the other sales were chain restaurants that sold in January 2008 to 2011 as a leased-fee

[5] We note several places in the appraisal reference the local sales as leased-fee transactions as well as fee-simple transactions.

transactions. Overall sales prices ranged from $1,150,000 to $3,400,000, or $138.60 to $386.28 per square foot. Ramsey adjusted the sale prices for market conditions, location, age/condition, and land to building ratio. Additionally, the leased fee sales were adjusted based on their relative NOI per square foot as compared to the subject property. Adjusted sale prices of the fee-simple sales range from $196.21 per square foot to $338.98 per square foot. The adjusted sales price of the leased-fee sales ranged from $294.01 to $323.71 per square foot. From both ranges of value, he chose a square foot price of $300 and opined a value of $1,750,000 as of January 1, 2011, using the sales approach to valuation.

Ramsey's Income Approach

The 2011 income approach was developed using an estimated market rent of $26.75 per square foot and effective gross income of $149,070 after vacancy and collection loss, to arrive at an NOI of $142,838 after management fee, replacement reserves, and other operating expenses. After considering three local sales, mortgage-equity technique, as well as a national survey, Ramsey chose an overall cap rate of 8.68%. We note the three sales used to extract a market cap rate were three of those also chosen by Lock. Based on these figures, Ramsey arrived at an indicated market value using the income approach for January 1, 2011 was $1,650,000.

Ramsey's appraisal notes his belief that the subject property should lease above the market range of $22.29 per square foot to $25.30 per square foot and below the range of $28.31 per square foot to $34.10 per square foot. Ramsey considered the subject property rent to be well below prevailing market level, which he attributes to the facts that the tenant took the space "as is," it's use would require a cash investment by the tenant and that it reflects the limited options of the prior tenant.

In reconciling his approaches, Ramsey found the income and cost approaches to value most reliable. He found the sales approach the least reliable because of the difficulty of obtaining sales that were recent, comparable, and directly indicative of the fee simple value of the subject property. He concluded a final value of $1,700,000 for January 1, 2011.

Neither of the appraisals supports the January 1, 2011, assessment. Lock's final fair market valuation was $1,500,000 and Nelson and Ramsey opined a fair market value of $1,700,000, whereas, the assessed value was $1,889,530 as of January 1, 2011. The Board of Review concedes on this point. O'Charley's will prevail in establishing over-assessment because both appraisals conclude a value less than the current January 1, 2011, assessment.

We find the appraisers are qualified, experienced, and knowledgeable. Furthermore, we find the appraisers both utilized essentially the same land sales in the cost approach and income information to establish their values. Furthermore, some of the comparable sales information was also the same. However, Lock completed a more extensive search sales transactions and included more sales in his comparison. He also considered sales outside the market area to verify the per-square-foot value he had concluded based on local market sales. This additional analysis gives more weight to his opinion.

Another main difference between the two appraisers was also their opinion of the market and the use of cap rates. Neither O'Charley's nor the Board of Review's appraisers were able to find land sales after 2007. Lock's data showed the national cap rate increasing steadily from prior to the assessment date in question and through that date. However, Lock testified new local leased-fee sales, indicated a lower cap rate for the subject property. The Board of Review believed this opinion was unfounded. The Board of Review was critical of Lock's appraisal because he previously appraised the property for the 2010 assessment and found that from 2009 to 2010 national cap rates were increasing and that local cap rates were therefore increasing. However, between 2010 and 2011 while national cap rates continued to increase, Lock decreased the local cap rate.

Ramsey's own information showed decreasing NOI between 2010 and 2011, but he calculated a decreasing cap rate. His information also tended to show a contraction in the restaurant industry.

Ramsey's appraisal, however, has the overall cap rate decreasing from 2010 to 2011, thus showing an increase in market value. But, the *Price Waterhouse Coopers* survey in Ramsey's appraisal has both the overall cap rate average and the exit cap rate average increasing between 2010 and 2011.

Ramsey's appraisal fails to convince this Board that his determination of value accurately reflects the market value for the subject property as of the assessment dates. We find Lock's appraisal is more reliable.

Conclusions of Law

The Appeal Board based its decision on the following law.

The Appeal Board has jurisdiction of this matter under Iowa Code sections 421.1A and 441.37A (2009). This Board is an agency and the provisions of the Administrative Procedure Act apply to it. Iowa Code § 17A.2(1). This appeal is a contested case. § 441.37A(1)(b). The Appeal Board determines anew all questions arising before the Board of Review related to the liability of the property to assessment or the assessed amount. § 441.37A(3)(a). The Appeal Board considers only those grounds presented to or considered by the Board of Review. § 441.37A(1)(b). But new or additional evidence may be introduced. *Id.* The Appeal Board considers the record as a whole and all of the evidence regardless of who introduced it. § 441.37A(3)(a); *see also Hy-vee, Inc. v. Employment Appeal Bd.*, 710 N.W.2d 1, 3 (Iowa 2005). There is no presumption that the assessed value is correct. § 441.37A(3)(a).

Property is to be valued at one hundred percent of its actual value. § 441.21(1)(a). Actual value is the property's fair and reasonable market value. *Id.* "Market value" essentially is defined as the value established in an arm's-length sale of the property. § 441.21(1)(b). Sales prices of the property or comparable properties in normal transactions are to be considered in arriving at market value. *Id.* If sales are not available or market value "cannot be readily established in that manner," "other factors" may be considered in arriving at market value. *Heritage Cablevision v. Board of*

Review of City of Mason City, 457 N.W.2d 594, 597 (Iowa 1990); Iowa Code § 441.21(2). "To determine whether other properties are sufficiently comparable to be used as a basis for ascertaining market value under the comparable-sales approach, [the Supreme Court] has adopted the rule that the conditions with respect to the other land must be 'similar' to the property being assessed." *Soifer v. Floyd County Bd. of Review*, 759 N.W.2d 775, 783 (Iowa 2009). "Similar does not mean identical, but having a resemblance; and property may be similar . . . though each possess various points of difference." *Id.* Determining comparability of properties is left to the "sound discretion" of the trier of fact. *Id.* Consideration should be given to size, use, location, and character, as well as the nature and timing of the sale. *Id.* This Board is "free to give no weight to proffered evidence of comparable sales which it finds not to be reflective of market value" *Heritage Cablevision*, 457 N.W.2d at 598.

In an appeal that alleges the property is assessed for more than the value authorized by law under Iowa Code section 441.37(1)(b), there must be evidence that the assessment is excessive and the correct value of the property. *Boekeloo v. Bd. of Review of the City of Clinton*, 529 N.W.2d 275, 277 (Iowa 1995).

Viewing the record as a whole, we determine the preponderance of the evidence supports O'Charley's claim of over-assessment as of January 1, 2011, as both appraisals conclude market values less than the current assessment. Based on the totality of the evidence, we find Lock's appraisal more reliable. Therefore, we modify the O'Charley's property assessment as determined by the Board of Review.

THE APPEAL BOARD ORDERS that the January 1, 2011, assessment of the O'Charley's property located in West Des Moines, Iowa, as determined by the Dallas County Board of Review, is modified to $1,500,000.

The Secretary of the State of Iowa Property Assessment Appeal Board shall mail a copy of this Order to the Dallas County Auditor and all tax records, assessment books and other records pertaining to the assessment referenced herein on the subject parcel shall be corrected accordingly.

Dated this 24 day of July 2012.

Jacqueline Rypma
Jacqueline Rypma, Presiding Officer

Richard Stradley, Board Chair

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Certificate of Service
The undersigned certifies that the foregoing instrument was served upon all parties to the above cause & to each of the attorney(s) of record herein at their respective addresses disclosed on the pleadings on 7-24, 2012
By: ✓ U.S. Mail ___ FAX
___ Hand Delivered ___ Overnight Courier
___ Certified Mail ___ Other
Signature ___